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Data Suggests Japan's Trade Surplus Has Peaked

There is evidence that the 75 percent appreciation of the yen since February 1985 is finally beginning to lower Japan's trade surplus. After 17 consecutive quarterly increases in the dollar figures, the surplus in the April-June 1987 period fell 5.3 percent from the year-earlier level to $20.6 billion (on a customs clearance basis). The decline reflected a 15.6 percent jump in imports to $36.3 billion, the highest in six years plus a deceleration of export growth (see Table 1). In yen terms, the trade surplus fell even more sharply (see Table 2).

The turnaround in volume terms actually began last year (see Table 3), but was outweighed by changes in currency values this spring. During the first half of 1987 export volume was down 2.1 percent from a year ago, while real imports were up 5.7 percent. The change in export volume, though, remains

Table 1: Japan's Total Trade in Dollar Terms

(in millions of dollars)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1982	$138,831	-8.7%	$131,931	-7.9%	$6,900
1983	146,928	5.8	126,393	-4.2	20,534
1984	170,114	15.8	136,503	8.0	33,611
1985	175,638	3.2	129,539	-5.1	46,099
1986	209,151	19.1	126,408	-2.4	82,743
1985: I	38,503	-1.3	32,513	-5.7	5,991
II	43,748	0.6	32,094	-7.0	11,654
III	43,909	2.7	31,239	-8.1	12,671
IV	49,478	10.3	33,693	0.5	15,785
1986: I	45,499	18.2	33,005	1.5	12,494
II	53,166	21.5	31,424	-2.1	21,742
III	54,768	24.7	30,153	-3.5	24,615
IV	55,718	12.6	31,826	-5.5	23,892
1987: I	51,478	13.1	31,939	-3.2	19,539
II	56,924	7.1	36,336	15.6	20,588

Table 2: Japan's Total Trade in Yen Terms

(in billions of yen)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1982	Y34,433	2.9%	Y32,656	3.8%	Y1,776
1983	34,909	1.4	30,014	-8.1	4,895
1984	40,325	15.5	32,321	7.7	8,004
1985	41,956	4.0	31,085	-3.8	10,871
1986	35,290	-15.9	21,551	-30.7	13,739
1985: I	9,898	9.5	8,340	4.3	1,559
II	11,025	11.1	8,093	2.8	2,932
III	10,591	2.4	7,534	-8.3	3,057
IV	10,442	-5.3	7,118	-13.6	3,323
1986: I	8,674	-12.4	6,334	-24.1	2,340
II	9,119	-17.3	5,399	-33.3	3,720
III	8,632	-18.5	4,758	-36.8	3,874
IV	8,865	-15.1	5,060	-28.9	3,805
1987: I	7,962	-8.2	4,953	-21.8	3,009
II	8,152	-10.6	5,201	-3.7	2,951

surprisingly modest in light of the sharp rise in the yen. The success of Japanese firms in maintaining market share reflects their strategy of passing on only a fraction of the yen's higher value. This policy, though, has taken a toll on export earnings; the yen value of exports was down almost 10 percent in the first half of the year.

Table 3: Change in Volume of Japan's Exports and Imports

		Exports	Imports
1982		-2.4%	-0.6%
1983		8.7	1.3
1984		15.4	10.7
1985		4.7	0.2
1986		-1.4	13.3
1985:	I	6.9	0.6
	II	6.8	-0.4
	III	4.0	-2.8
	IV	1.8	3.3
1986:	I	-0.2	3.6
	II	-0.9	16.8
	III	-0.3	18.6
	IV	-4.2	14.4
1987:	I	-0.1	8.1
	II	-3.9	3.6

Despite the signs of progress, Japan's trade surplus in 1987 is likely to surpass last year's $82.7 billion. For the first six months the trade imbalance was $40.1 billion in Japan's favor, up from $34.2 billion in the first half of 1986. Nomura Research Institute, for example, is predicting that Japan's surplus will rise $2.5 billion in 1987.

Japan's surplus in merchandise trade, services and transfers (i.e. the current account) in 1986 was equivalent to 4.4 percent of the nation's gross national product. Tetsuo Kaneko, director general of the Economic Planning Agency, told the Diet in May that it would be reasonable to have a surplus equal to 2 percent, which would amount to about $50 billion at current exchange rates. A decline to such a level, though, will probably require several years. Since the country's exports are 65 percent higher than its imports, purchases of foreign goods must increase at a considerably faster pace than exports simply to prevent the surplus from rising. In addition, the income elasticity of import demand (the percentage increase in imports resulting from a 1 percent rise in income) is lower in Japan than in most other countries. If Japan grows at the same rate as other countries (as forecast by the Organization for Economic Cooperation and Development for 1987-88), the income elasticity effect may overcome the impact of the strong yen, widening the country's trade surplus. Of course, a sudden rise in the price of oil could quickly reduce the surplus. According to one estimate, if oil prices returned to their 1974-85 average real level, it would add $90 billion to Japan's import bill.

Table 4: Japan's Trade with the United States in Dollar Terms

(in millions of dollars)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1982	$36,330	-5.9%	$24,179	-4.4%	$12,151
1983	42,829	17.9	24,648	1.9	18,181
1984	59,937	39.9	26,862	9.0	33,075
1985	65,278	8.9	25,793	-4.0	39,485
1986	80,456	23.3	29,054	12.6	51,402
1985: I	13,346	6.8	6,771	1.3	6,575
II	16,837	9.0	6,641	-1.6	10,196
III	16,615	5.4	6,111	-9.8	10,504
IV	18,480	13.9	6,270	-5.7	12,211
1986: I	16,696	25.1	6,278	-7.3	10,418
II	20,921	24.3	8,305	25.1	12,616
III	21,280	28.1	7,525	23.1	13,755
IV	21,559	16.7	6,946	10.8	14,613
1987: I	18,003	7.8	6,961	10.9	11,042
II	21,183	1.3	7,583	-8.7	13,600

Table 5: Japan's Trade with the United States in Yen Terms

(in billions of yen)

	Exports (f.o.b.)	Change Over Year-Earlier Period	Imports (c.i.f.)	Change Over Year-Earlier Period	Trade Balance
1982	Y9,015	5.8%	Y5,991	7.9%	Y3,025
1983	10,179	12.9	5,855	-2.3	4,323
1984	14,221	39.7	6,364	8.7	7,858
1985	15,583	9.6	6,213	-2.4	9,369
1986	13,564	-13.0	4,918	-20.8	8,646
1985: I	3,429	18.3	1,737	11.9	1,692
II	4,244	20.4	1,674	8.8	2,569
III	4,008	5.2	1,474	-10.0	2,534
IV	3,903	-2.1	1,328	-18.7	2,575
1986: I	3,191	-6.9	1,203	-30.7	1,988
II	3,589	-15.4	1,421	-15.1	2,168
III	3,355	-16.3	1,190	-19.3	2,165
IV	3,429	-12.1	1,104	-16.9	2,325
1987: I	2,786	-12.7	1,079	-10.3	1,707
II	3,034	-15.5	1,084	-23.7	1,950

The prospects for a decline in Japan's surplus with the United States are not as bright. Although Assistant Treasury Secretary David Mulford has predicted a $7 billion improvement this year, the imbalance was $24.6 billion in the first half of this year, up from $23 billion last year (see Table 4 and 5). While European Community exports to Japan are running about 32 percent ahead of last year, U.S. shipments were down 0.3 percent in the first half of 1987. It should be noted, though, that Japan's imports from this country were unusually high in the January-June 1986 period due to large purchases of gold. One positive sign is that Japan's shipments to this country fell below the year-earlier level in June for the first time in 27 months, largely as a result of a 17.8 percent fall in motor vehicle exports.

Randall S. Jones

Japan-EC Conference Focuses On Trade

The bilateral trade situation dominated the July 9-10 semiannual meeting between Japan and the European Community. Both sides sought major concessions, but ended up mostly empty-handed. Common ground was only found on one trade-related area, though support for cooperation in science and technology was reiterated across a broad spectrum. The two sides came away from the meeting with sharply different outlooks, presaging continued frictions over trade.

In the face of almost certain criticism, Tokyo nevertheless reiterated its previous positions that EC exports of goods and services will receive non-discriminatory treatment, that exporters must exert more effort to penetrate the Japanese market, and that there will be no set goals for increased purchases of EC products. Japanese representatives also hit the community's late May decision to extend punitive tariffs to parts as well as finished products imported from Japan, claiming that the policy violates the General Agreement on Tariffs and Trade. But the EC is unhappy with the "screwdriver" factories several Japanese firms have established in Europe, and adopted the [illegible] to force Japanese assembly plants to increase the local content of their output. Tokyo also asked for a hike in EC import quotas on 108 items. On a more positive note, Japan agreed to increase access for European exports of medical equipment, pharmaceuticals and cosmetics.

The EC delegation, led by director general of external relations Leslie Fielding, was much more strident in its demands. Pointing to the growing trade deficit ($10.5 billion in the first half of the year, 26.4 percent above the same period last year), Mr. Fielding demanded "deeds, not words." He presented a list of world-class EC products, including aircraft and medical, electric and telecommunications equipment, asking that Tokyo allocate $1 billion to specifically reduce the bilateral trade imbalance. A drastic move is necessary, he charged, because of Tokyo's "dangerously slow" pace of liberalization. Japanese officials responded that imports of EC products had grown faster than exports during the first half of the year (32.3 percent versus 28.9 percent in dollar terms), a trend they expected to continue and thus reduce the imbalance. Even so, the EC pointed out that the deficit could widen to over $20 billion for all of 1987, far above 1986's $16.7 billion level.

The EC also lamented the negative impact of the U.S.-Japan semiconductor agreement on European prices for memory chips. The higher prices have hurt EC

question is whether the proposal can withstand the presidential veto that the administration has promised. (Last year, the House failed to override a veto by just eight votes.) This time, the Democratic-controlled Congress is gearing up to gain as much political mileage from the confrontation as possible. There is even some talk of scheduling the override vote to coincide with "Super Tuesday" next March, when several textile-producing states in the South will hold presidential primaries.

A tactic like this may be necessary if legislators want HR 1154 to become law. According to one report, the House is still roughly 45 votes short of the requisite two-thirds majority for an override. In the Senate, supporters are also fighting against the odds right now. Still, a confluence of constituent considerations, economic factors and presidential campaign concerns could swing the vote against Mr. Reagan's veto.

Eileen Marie Doherty

Notes

Senate Trade Bill - After a month's debate the Senate approved S 1420, the omnibus trade package, on July 21 by an overwhelming 71-27 vote. Despite last-minute White House appeals to GOP legislators to oppose the bill, 19 Republicans joined 52 Democrats in casting a "yes" vote. All of the 27 who opposed the bill were Republicans. The administration wasted no time after the bill's passage in threatening to veto the legislation unless the final product is changed. At present, it appears that Congress stands a fair chance of overriding that veto; both the House and the Senate bills passed with more than the requisite two-thirds majority needed for an override. Still, some legislators have warned that they will change their vote to a "no" on the final bill if significant changes are not made during the conference committee. A detailed discussion of the provisions of the bill will be included in the next issue of JEI Report.

Specialty Steel - President Reagan has defied conventional economic wisdom and extended the import shield for U.S. specialty steel makers through September 30, 1989 (see JEI Report No. 24B, June 26, 1987). The White House justified its July 16 decision by citing "persistent global overproduction" of stainless steel and alloy tool steel, some of which it claimed is subsidized, as well as "trade barriers and distortive practices used by [U.S.] trading partners to protect their domestic industries and to stimulate exports." A spokesman noted that the same factors had persuaded the president in July 1983 to give domestic manufacturers four years of protection. But then as now the administration clearly hoped that its move would help contain protectionist pressures on Capitol Hill.

The new specialty steel protection plan is a modified version of the one that expired July 19. Flat-rolled products, which represented two-thirds of 1986 specialty steel imports, will continue to be subject to tariffs on top of the statutory rates of 9.5 percent or 10 percent for stainless sheet and plate and 8 percent to 11.5 percent for stainless steel strip. For all three products the extra duties will be 3 percent over the next 12 months and 1 percent in the final 15-month stretch of the relief period (see Table). Under the old program

the added tariffs started at either 10 percent (sheet and plate) or 8 percent (strip) and dropped in stages to 4 percent during the July 20, 1986-July 19, 1987 period. Canada and Sweden, however, will still be the only important suppliers of flat-rolled products affected by the extra duties since shipments from the European Community (including Spain and Portugal), Japan and 14 other countries are covered by quotas under the White House's overall steel restraint program, which runs through September 1989.

Similarly, imports of stainless steel bar and rod and alloy tool steel will remain capped by quotas, although the limits will be raised over the course of the relief period (see Table). Allocations will again be negotiated with major suppliers, including Japan -- the top supplier of bar and rod and the number-two source of alloy tool steel -- and Sweden. Spain, the third-largest shipper, is also on the list because it joined the EC after the group agreed to restrict U.S.-bound steel shipments through September 1989. (In addition to imports from EC-10 countries, deliveries of bar, rod and tool steel from Austria and Brazil are outside the new restraint program since they are governed by other arrangements.) Since it will take time to work out the new quota allotments, the White House has extended the July 20, 1986-July 19, 1987 country allocations for 90 days.

New Specialty Steel Protection Program

Extra Tariffs

	7/20/87-7/19/88	7/20/88-7/19/89	7/20/89-9/30/89
Stainless Steel Sheet and Strip	3%	2%	1%
Stainless Steel Plate	3	2	1

Quotas

(in tons)

	7/20/87-10/19/87	10/20/87-7/19/88	7/20/88-7/19/89	7/20/89-9/30/89
Stainless Steel Bar	5,738	17,717	24,159	4,977
Stainless Steel Rod	3,307	10,213	13,926	2,869
Alloy Tool Steel	4,271	13,182	17,977	3,703

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The views expressed in this report are those of the authors and do not necessarily represent those of the Japan Economic Institute.